



Director of
Central
Intelligence

Top Secret

OCPAS/CIG

CY# 285

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National Intelligence Daily

25X1

**Wednesday
1 August 1984**

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CPAS NID 84-179JX

1 August 1984

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NICARAGUA:**Worsening Financial Problems**

Living standards are continuing to deteriorate in Nicaragua, and the government's growing insolvency suggests that even tighter austerity is in the offing. [redacted]

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A source of the US Embassy in Managua reports that the junta has already spent all the foreign exchange earned from the harvest last spring. To finance immediate needs, the government has resorted to selling—at a discount—crops that will not be harvested until November. [redacted]

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Foreign bankers are becoming increasingly intolerant of the junta's repeated late payments and attempts to rewrite debt rescheduling agreements. [redacted]

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Mismanagement, coupled with military activity and labor shortages in farm areas, has caused shortages of beans, rice, and other basic foods to spread from urban areas to the countryside. A government official told US Embassy officers that large-scale purchases of foreign grain will be required soon. Shortages of foreign exchange to buy parts and raw materials have forced some industrial firms to close. [redacted]

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Comment: [redacted]

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The need to import more grain suggests that foreign exchange allocations to Nicaragua's industrial sector will have to be cut back further, which in turn will boost urban unemployment and make even more consumer goods unavailable. Much of the populace appears to lay the blame for its declining living standards primarily at the government's doorstep, despite the regime's claims that economic problems are the fault of US policy. [redacted]

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NEW ZEALAND-US: Ban on Ship Visits

Prime Minister David Lange on Monday reiterated the Labor Party's platform pledge to ban visits by US naval ships, but Wellington's actual policy on the issue will evolve slowly over the next six months. [redacted]

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The ban reflects the party's concerns over nuclear propulsion and its opposition to the longstanding US policy of not revealing whether visiting US ships carry nuclear arms. Last week Lange also reiterated the party's pledge to renegotiate the ANZUS alliance. [redacted]

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Comment: Lange is required by party policy to support Labor's official platform, despite his personal support for ANZUS and his reported eagerness to find a compromise policy on nuclear-armed vessels. He may believe that reiterating the Labor platform will undercut charges by the Labor Party's left wing that he is a "puppet" of Washington. [redacted]

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Although elected with a strong parliamentary majority, Lange's personal support within the party is spotty, and his ability to move it along more moderate lines is still doubtful. He is viewed suspiciously by Labor's left wing, including party president Jim Anderton. [redacted]

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Lange and party moderates will have an opportunity to change the platform at Labor's annual conference in September. In the meantime he probably is hoping to put ANZUS—and the issue of US ship visits—on the back burner in order to tackle economic issues and to consolidate public support for his government. [redacted]

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Lange has said that he will address foreign policy issues after dealing with the economy—which may defer a policy debate on ANZUS until early next year. His political position then—and his ability to control Labor's left wing—will reflect his success at addressing New Zealand's serious economic problems. [redacted]

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**EAST GERMANY-
WEST GERMANY:****Summit in Doubt**

Disagreement between Bonn and East Berlin on protocol questions—and Soviet misgivings—still may prevent the planned visit to West Germany next month by East German leader Honecker. [REDACTED]

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Pravda on Friday accused the Kohl government of using economic leverage to meddle in East German affairs. The article emphasized Bonn's failure to act on longstanding East German demands for fuller recognition as a permanent and legitimate state. It did not mention, however, the recently announced loan, East German travel concessions, or the Honecker trip. [REDACTED]

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East German media replayed the *Pravda* article on Saturday but on Monday printed a Hungarian article that lauded East Berlin's dialogue with the West. The latter article discussed recent visits to East Germany by Greek, Italian, and Swedish leaders as well as intra-German relations. [REDACTED]

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Comment: The *Pravda* commentary probably has made it harder to settle differences over the trip by emphasizing that a visit by Honecker to Bonn would imply recognition of East German sovereignty. East Berlin probably will cite the article to argue that Kohl should make this symbolic but important concession. [REDACTED]

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Pravda's allegation that Bonn uses economic leverage will tend to reduce East Berlin's flexibility, particularly in view of Bonn's explicit linkage last week of its loan with travel concessions by East Germany. The East Germans probably intend the replay of the Hungarian article to indicate to Bonn that they still want the visit to go ahead but only if the conditions are right. [REDACTED]

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VENEZUELA: Skyjacking

The two terrorists killed yesterday morning when Venezuelan commandos recovered a hijacked Venezuelan civil aircraft were members of the Democratic Movement for the Liberation of the Haitian People. The organization apparently was formed in Caracas during 1982 and includes Haitians, Dominicans, Venezuelans, and Colombians. It first came to public attention in December 1982 when it attempted to smuggle firearms into Santo Domingo. [REDACTED]

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Comment: The stated goal of the Movement is the overthrow of the Jean-Claude Duvalier regime in Haiti. It is a small part of a large but disorganized Haitian exile community. These groups plot continuously, but they have yet to mount a successful attack. Neither the Movement nor any other Haitian exile group appears to pose a serious threat to the Haitian Government. [REDACTED]

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JAPAN: Tight Budget Set

The Japanese Cabinet yesterday approved budget ceilings for FY 1985 that will allow an overall government spending increase of less than 1 percent, with most ministries facing a 10-percent cut. Defense, with a spending cap of 7 percent, and foreign aid—11.4 percent—are major exceptions in the austere budget designed to control persistent deficits. [REDACTED]

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Comment: The ceilings provide guidelines for budget planning, which concludes in December with Cabinet approval of a final draft. Although the Defense Agency may not get the full 7-percent increase, Tokyo probably hopes the ceiling—double what the Finance Ministry had pushed for—will win points in Washington. The high cap on defense spending probably will touch off sharp domestic criticism from the press and opposition parties. The persistent weakness of the yen vis-a-vis the dollar—which is boosting Japan's exports and its competitiveness in world markets—has aided Finance Ministry efforts to hold down spending. Prime Minister Nakasone's political rivals, however, probably will continue to blame his austere fiscal policy for slower growth and trade friction with Japan's major trading partners. [REDACTED]

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GUATEMALA: New Assembly Opens

The Constituent Assembly will be installed today amid indications that extreme rightists will be unable to secure their demand for immediate selection of a provisional president. Recounts have given two additional seats to the ultrarightist National Liberation Movement, which will have the largest single block of votes with 23 seats. Centrist parties, however, will still have a majority in the 88-member body. Meanwhile, the US Embassy reports that the three major political parties have agreed to share the presidency of the Assembly on a rotating basis. [REDACTED]

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Comment: The parties are almost uniformly satisfied that the voting on 1 July was conducted honestly and without interference from the military. This, coupled with the failure of the right to control the Assembly, suggests that most deputies initially will concentrate on writing a new constitution in preparation for national elections next year, as Chief of State Mejia has directed. Mejia's hand also appears strengthened by distrust among the parties, as illustrated by their apparent desire to prevent any one party from using the Assembly presidency to strengthen its election prospects next year. [REDACTED]

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In Brief**Africa**

- **Angolan** press reports **East German** and Angolan merchant ships severely damaged in Luanda harbor by US-made mines . . . UNITA claiming credit, but **South Africa** may be responsible for attack intended to benefit insurgents. [REDACTED]

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Middle East

- **Israeli** Prime Minister Shamir and Labor leader Peres meet today to discuss government of national unity . . . each still prefers to form own coalition . . . five key Knesset members, including former Defense Minister Weizman, yesterday reaffirmed preference for unity government. [REDACTED]

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- [REDACTED] **USSR's** first delivery of SA-9 surface-to-air missiles to **South Yemen** . . . widely exported mobile system will further improve Aden's growing air defense capability . . . South Yemen received first SA-6 SAMs last year. [REDACTED]

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- US Embassy reports **Soviet** Ambassador to **Seychelles** hinting Moscow intends to seek military privileges at least equal to those of US . . . complaining to President Rene that USAF tracking station receives military information from satellites targeted against USSR. [REDACTED]

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Special Analysis

PAKISTAN-USSR: Zia's Response to Military Pressure

The USSR's recent strong demarche charging Pakistan with complicity in the Afghan resistance indicates that Moscow may undertake cross-border operations. In this event, Islamabad could contain airstrikes or brief shallow incursions—the most likely Soviet measures—and there would be little impact on Pakistani support for the insurgents. President Zia would attempt to avoid broader military confrontation while cultivating international support. If the Soviets persisted, however, he probably would need both US diplomatic and military assistance—short of US forces—to help him maintain his resolve.

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Soviet forces now in Afghanistan are capable of conducting limited operations against Pakistan such as pursuing fleeing insurgents, attacking suspected arms convoys approaching the border, and undertaking air or artillery strikes on suspected insurgent camps.

- The Soviets could mount operations up to regimental size using air assault teams or ground forces supported by fighter-bombers and helicopters against insurgent bases in Pakistan.

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The Soviets are more likely to resort to air operations than ground attacks because they would cause fewer casualties and international repercussions. Air operations, however, would be less effective.

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Any sustained campaign would require sending additional forces to Afghanistan or shifting the troops already there.

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Pakistani Military Response

Zia would react to Soviet hot pursuit by directing Pakistani forces to resist attack but not to seek engagement unless the intrusions became more than isolated incidents. He believes that the Soviets cannot be appeased and that their presence in Afghanistan directly threatens Pakistan's security, but he, nevertheless, wants to avoid a military confrontation.

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Pakistani ground units could inflict losses on small Soviet or Afghan forces during chance encounters and, given warning, cause greater casualties with planned ambushes. The Pakistanis lack the mobility, however, to respond quickly to unexpected rapid raids into remote areas.

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Political Impact

Repeated Soviet incursions would renew debate among Pakistani officials about policy toward Afghanistan. Zia could seek to satisfy critics without surrendering any ground by making token concessions to the Soviets such as restricting insurgent propaganda activities and closing their more visible offices in Peshawar. He is already reported to have ordered the resistance parties to move out of the city by 31 August. If true, this may well be a gesture responding to Soviet demarches.

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Zia would probably attempt to use the incursions to increase international pressure on Moscow. He would reiterate that Islamabad provides only safehaven to displaced refugees and that it is demonstrating its commitment to a diplomatic solution by participating in the UN's indirect peace talks in Geneva.

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If the Soviets persist in cross-border operations, Zia would ask for American diplomatic and military assistance although he would not expect the US to send troops. The US response would influence substantially his ability to withstand pressure within the government for concessions to the Soviets.

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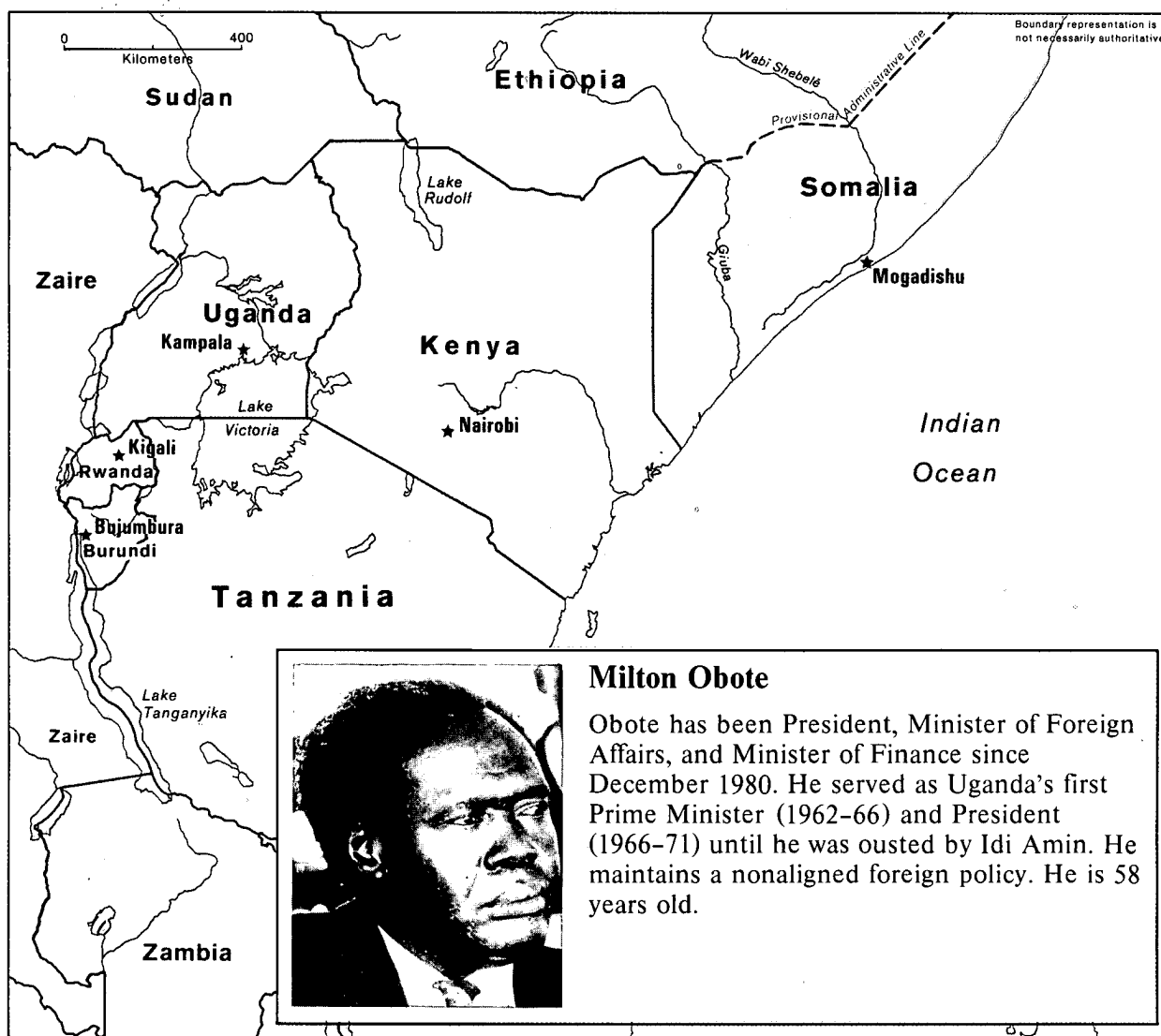
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**Milton Obote**

Obote has been President, Minister of Foreign Affairs, and Minister of Finance since December 1980. He served as Uganda's first Prime Minister (1962-66) and President (1966-71) until he was ousted by Idi Amin. He maintains a nonaligned foreign policy. He is 58 years old.

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Special Analysis**UGANDA:****Instability Increasing**

Security in Uganda has deteriorated in recent months, raising the specter of prolonged instability that could offer North Korea, Cuba, or the USSR new opportunities to meddle in the country. President Obote's grip is slipping although he is likely to survive until the elections in December 1985, if only because his opponents are weak. He, nevertheless, is likely to have to cope with growing military lawlessness, government indecision, and increasing economic desperation.

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The government's control over the military has slackened badly since the death of Chief of Staff Ojok, Obote's close ally. Lack of discipline has left the Army ineffective against the several guerrilla groups although they do not now pose a direct threat to the government. Moreover, the Army's ineptitude and brutality toward civilians are undermining popular support for Obote's regime.

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Obote's rivals are building political bases of support, and relations between him and some of his ministers are poor.

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The improvement in the economy has been Obote's main accomplishment since taking office in 1981, but deteriorating security now threatens that progress. Prolonged violence would disrupt agricultural production, transportation, and marketing. It also could cause aid donors to cut their assistance, which has averaged \$275 million annually in the past three years.

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Obote will ask the UK and the US for more military and economic aid. If he believes his needs are not being met, he will not hesitate to expand military ties with North Korea or turn to Cuba and the USSR. All are likely to give only token aid.

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A coup could push Uganda quickly to the left. Almost any successor would be likely to establish closer ties with the Communist states. This would cause new concern in Kenya, Sudan, and Zaire about their borders and might prompt them to ask the US for increased military aid.

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